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NSC FOR DAN FISK, CINDY PENDLETON

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SUBJECT: CORRECTED COPY - MEXICO ECONOMIC NOTES, MARCH
16-23, 2007

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Corrected copy. See reference to USD 50 billion in para 3.

Summary

¶1. (SBU) The Mexican Chamber of Deputies (lower house) on March 22 approved new draft legislation to reform the agency responsible for providing pension and health care services for government employees. The centerpiece of the reform is the replacement the current "defined-benefits" system with a defined-contribution scheme (individual retirement accounts) -- similar to the system created in 1997 for private sector employees. President Calderon on March 18 gave a frank speech about the challenges facing Mexico in the petroleum sector, and said that the country has less than ten years of reserves remaining at current production rates. A DOT-GOM monitoring group on the cross border trucking pilot program is making progress on working out lingering issues regarding Mexican companies, participation in the program and creating guidelines for how U.S. companies will apply to take part in the second phase of the pilot. The President and the Governor of Baja California inaugurated a NADBank-financed wastewater treatment plant in Mexicali. As a part of the government's strategy to strength its debt structure, Mexico on March 15 sold warrants that allow investors to swap foreign bonds worth USD 2.66 billion for fixed-rate peso-denominated bonds in September, October, and November. The IPC stock index rose 3% to 29,220 on March 21 on news from the U.S. Federal Reserve about interest rates. End Summary.

Government Advances Long-Awaited Pension Reform

12. (U) The Mexican Chamber of Deputies (lower house) on March 22 approved new draft legislation to reform the agency responsible for providing pension and health care services for government employees. Amid protests both inside and outside the building, the 500-member Chamber voted 313-146 with two abstentions in favor of the bill. Local press reports say the Senate could approve the reform proposal as early as March 27. The reform would gradually raise the retirement age and replace the current "defined-benefits," pay-as-you-go pension system with a defined-contribution scheme (individual retirement accounts) -- similar to the system created in 1997 for private sector employees. To make the proposal more palatable to Mexico's powerful unions, the bill doubles the size of the minimum guaranteed pension and increases government contributions to some of the agency's funds. Although the proposal seems assured of more than enough votes for passage, the Democratic Revolution Party (PRD) and some unions are opposing it -- arguing that it will lead to the privatization of social security for state workers. This reform would relieve significant pressure on government finances and would be the first major economic reform passed under the Calderon administration. See reftel for more information on this reform.

Calderon's Discusses Challenges to Petroleum Sector

13. (U) On Pemex Day, March 18, the 69th anniversary of the expropriation of foreign oil company assets, President Calderon spoke frankly about the challenges facing Mexico in the petroleum sector. He announced that Mexico has less than ten years of reserves remaining at current production rates,

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that in past years Pemex has operated below the industry standard of replacing 100 percent or more reserves, and that Pemex has more than USD 50 billion in pension liabilities alone. Calderon noted that oil income will be essential for funding future government spending on poverty and infrastructure, and he concluded that if Mexico "did not act soon to reverse the situation, the country would face severe problems." While pundits and industry participants have described Mexico's oil woes at length, this is the first time a Mexican President has outlined the situation in such stark terms. Post will report on the speech and reaction to it septel.

USG Officials Discuss the Trucking Pilot Program

14. (SBU) On March 21, Econoff met with Secretariat of Communication and Transportation (SCT) and Economia officials to conduct a video conference with the Department of Transportation on the cross border trucking pilot program. The group is making progress on working out lingering issues regarding the Mexican companies participating in the program and creating guidelines for how U.S. companies will apply to participate in the second phase of the pilot. The SCT noted that there is significant pressure from Mexican carriers and the business community to address chronic border crossing issues, such as long wait times, parallel to implementing the pilot program.

NADBank Opening a Sewage Treatment Plant

15. (U) President Calderon and Governor of Baja California Eugenio Elorduy have inaugurated the Las Arenitas Wastewater Treatment Plant in Mexicali. The project is part of a wastewater improvements project certified by the Border Environment Cooperation Commission (BECC) in September 2003 and financed with grants from the North American Development Bank (NADBank). The project is estimated to cost just over

USD 30 million, and was partially financed with a USD 12.85 million construction grant from the Border Environmental Infrastructure Fund (BEIF), which is funded by EPA and administered by NADBank. The plan will provide service to almost 175,000 people in Mexicali and eliminate discharges of untreated wastewater into the New River, which flows into the U.S.

Mexico Continues To Whittle Down its Foreign Debt

¶6. (U) As a part of the government's strategy to strength its debt structure, Mexico on March 15 sold warrants that allow investors to swap foreign bonds worth USD 2.66 billion for fixed-rate peso-denominated bonds in September, October, and November. The auction attracted demand to exchange more than USD 3.5 billion with respect to the dollar-denominated warrants and approximately 530 euros for the euro-denominated bonds. The Secretariat of Finance's Director of Public Credit, Gerardo Rodriguez, said publicly that the government planned to wait until all the warrants come due late this year before deciding whether to sell more.

Stocks Climb on Positive News From the U.S.

¶7. (U) Mexican stocks rose the most in five months as the U.S. Fed Open Market Committee signaled that it will consider

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cutting rates by the June policy meeting, easing concern that higher borrowing costs will hurt demand in Mexico's largest export market. The IPC stock index rose 3% to 29,220 on March 21, surpassing for the first time closing level of February 26, the day before a 9-percent decline in Chinese share prices sparked a global selloff.

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